

Tennessee Education Lottery
Revenue and Proceeds Projections

FY 2005-2006
FY 2006-2007

Presented to:
The State Funding Board

By:
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PRESENTATION OUTLINE

- I. FY05-06 Estimates – November 30, 2005**
- II. Actual-to-Estimates**
- III. Explanation for Differences**
- IV. FY05-06 Estimates – Revised**
- V. FY06-07 Assumptions**
- VI. FY06-07 Estimates – Revised**
- VII. Final Comments**

I. FY05-06 ESTIMATES
NOVEMBER 30, 2005

Revenue Source	Lower Estimates	Mean Estimates	Upper Estimates
Instant Games	\$556,863,821	\$566,768,619	\$576,673,418
Cash 3	\$56,557,574	\$57,269,113	\$57,980,652
Powerball	\$155,042,307	\$165,537,902	\$176,033,497
Lotto 5	\$21,263,102	\$22,692,740	\$24,122,379
Cash 4	\$24,454,541	\$24,755,084	\$25,055,627
Misc.	\$5,000,000	\$5,000,000	\$5,000,000
Net Revenues	\$819,181,345	<u>\$842,023,458</u>	\$864,865,573
Expenses @ 72%	\$589,810,568	\$606,256,890	\$622,703,213
Proceeds @ 28%	\$229,370,777	<u>\$235,766,568</u>	\$242,162,360

II. ACTUAL – to – ESTIMATES

Revenue Source	Where we expected to be on 03/31/2006	Actual Net Sales thru 03/31/2006
Instant Games	\$425,076,464	\$474,913,940
Cash 3	\$42,951,835	\$45,847,592
Powerball	\$124,153,427	\$150,713,408
Lotto 5	\$17,019,555	\$16,472,541
Cash 4	\$18,566,313	\$19,421,166
Misc.	\$3,750,000	\$3,691,092
Total Net Revenues	\$631,517,594	\$711,059,739
Expense Ratio	72%	70.83%
Total Expenses	\$454,692,668	\$503,670,671
Proceeds Ratio	28%	29.17%
Net Lottery Proceeds	\$176,824,926	\$207,389,068

III. EXPLANATION for DIFFERENCES

Net Revenues - 12.6% higher than expected

POWERBALL

- Sales have been 21.4% higher than expected
- *Matrix change on August 31, 2005*
- Statistically more difficult to win the jackpot
- Allows for higher jackpots
- Allows for increased frequency of higher jackpots
- 8 months prior – 5 drawings where the jackpot was over \$100.0 million
 - 1 over \$200.0 million
 - 0 over \$300.0 million
- 8 months after – 27 drawings where the jackpot was over \$100.0 million
 - 9 over \$200.0 million
 - 4 over \$300.0 million
- 8 months prior – Average Weekly Sales = \$2,483,843
- 8 months after – Average Weekly Sales = \$4,323,636

CASH 3

- Sales have been 6.7% higher than expected
- *Introduction of Mid-Day Drawings*
- Two drawings per day
- Began on November 21, 2005
- 23 weeks prior – Average Weekly Sales = \$1,067,017
- 23 weeks after – Average Weekly Sales = \$1,272,762

III. EXPLANATION for DIFFERENCES - CONTINUED

CASH 4

- Sales have been 4.6% higher than expected
- *Introduction of Mid-Day Drawings*
- Two drawings per day
- Began on November 21, 2005
- 23 weeks prior – Average Weekly Sales = \$467,401
- 23 weeks after – Average Weekly Sales = \$522,606

INSTANT GAMES

- Sales have been 11.7% higher than expected
- (1) *TELC has utilized a Higher Prize Payout Ratio*
- (2) *More Frequent and Higher POWERBALL Jackpots*
- (3) *Mid-Day Drawings for CASH 3 and CASH 4*
- Customers make incremental purchases
- 12 weeks prior to the POWERBALL matrix change:
 - Average Weekly Sales = \$11,811,871
- 12 weeks after the POWERBALL matrix change, but prior to the introduction of Mid-Day Drawings:
 - Average Weekly Sales = \$12,495,693
- Since the introduction of Mid-day Drawings:
 - Average Weekly Sales = \$14,547,490

III. EXPLANATION for DIFFERENCES - CONTINUED

Total Expenses - 10.8% higher than expected

- **As sales increase...expenses increase**
- **Majority of lottery expense categories are some fixed percentage of sales**
- **Prize Expense = 54.7% of gross ticket sales (58.7% of net ticket sales)**
- **Retailer Commissions = 6.5% of gross ticket sales (7.0% of net ticket sales)**
- **Vendor Fees paid to GTECH Corporation and Scientific Games are 1.24% and 1.14% of adjusted sales respectively.**
- **Given that the expense ratio is currently below our expectations (70.83%) and revenues are above our expectations (12.6%), this is not affecting net lottery proceeds in a negative manner.**

Net Lottery Proceeds - 17.3% higher than expected

- **Growth of net revenues has been better than expected**
- **Expense growth has been lower than revenue growth**
- **Revenue Growth Rate (12.6%) > Expense Growth Rate (10.8%) \approx Proceeds Growth Rate (17.3%) > Sales Growth Rate (12.6%)**

IV. FY05-06 Estimates - REVISED

Revenue Source	Lower Estimates	Mean Estimates	Upper Estimates
Instant Games	\$622,665,000	\$627,150,000	\$634,859,000
Cash 3	\$61,282,000	\$61,523,000	\$61,763,000
Powerball	\$189,282,000	\$196,282,000	\$203,281,000
Lotto 5	\$21,057,000	\$21,282,000	\$21,506,000
Cash 4	\$25,677,000	\$25,780,000	\$25,884,000
Misc.	\$4,900,000	\$5,000,000	\$5,100,000
Net Revenues	\$924,863,000	<u>\$937,017,000</u>	\$952,393,000
Expenses @ 71.5%	\$661,277,000	\$669,967,000	\$680,961,000
Proceeds @ 28.5%	\$263,586,000	<u>\$267,050,000</u>	\$271,432,000

Net Revenue Estimate increased by 11.3%
Total Expense Estimate increased by 10.5%
Net Lottery Proceeds Estimate increased by 13.3%

V. FY06-07 ASSUMPTIONS

- **Used the Revised Estimates for FY05-06 as a base**
- **2.0% annual growth**
- **Growth rate approximates the compound annual growth rate for the industry over a ten-year period.**
- **Prize Expense, as a percent of net revenues, will increase slightly.**
- **Expense Ratio = 72.0% of net revenues**
- **Proceeds Ratio = 28.0% of net revenues**

VI. FY06-07 Estimates – REVISED

Revenue Source	Lower Estimates	Mean Estimates	Upper Estimates
Instant Games	\$635,118,000	\$639,693,000	\$647,556,000
Cash 3	\$62,508,000	\$62,753,000	\$62,999,000
Powerball	\$193,067,000	\$200,207,000	\$207,347,000
Lotto 5	\$21,478,000	\$21,707,000	\$21,936,000
Cash 4	\$26,190,000	\$26,296,000	\$26,402,000
Misc.	\$4,998,000	\$5,100,000	\$5,202,000
Net Revenues	\$943,359,000	<u>\$955,756,000</u>	\$971,442,000
Expenses @ 72%	\$679,218,000	\$688,144,000	\$699,438,000
Proceeds @ 28%	\$264,141,000	<u>\$267,612,000</u>	\$272,004,000

Net Revenue Growth: 2.0% (\$18.7 million)
Total Expense Growth: 2.7% (\$18.2 million)
Net Lottery Proceeds Growth: 0.2% (\$562,000)

VII. FINAL COMMENTS

- **If...our Net Revenue estimates for FY05-06 turn out to be accurate...**
- **If...Total Expenses for FY05-06 turn out to be 71.5% of Net Revenues...**
- **If...Total Expenses for FY06-07 increase to 72.0% of Net Revenues...**
- **Then...net sales must grow by at least 1.79% (approximately \$16.7 million) just for net lottery proceeds to remain constant from FY05-06 to FY06-07.**
- **Breakeven-point given these assumptions.**

Incremental Proceeds over FY05-06	Proceeds Growth	Incremental Revenue over FY05-06	Net Sales Growth
(\$750,000)	-0.28%	\$14,055,000	1.50%
\$0	0.00%	\$16,773,000	1.79%
<u>\$562,000</u>	0.21%	<u>\$18,740,000</u>	<u>2.00%</u>
\$8,433,000	3.16%	\$46,851,000	5.00%
\$14,992,000	5.61%	\$70,276,000	7.50%
\$21,551,000	8.07%	\$93,702,000	10.00%